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Panama After Operation Just Cause  
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¶1. (SBU) Since the 1989 restoration of democracy, Panama has established and consolidated a democratic, stable and responsive government; accelerated economic growth through open markets; and worked to ensure that the benefits of that growth reach all citizens. While a hemispheric leader in progress on these fronts, Panama today stands at a crossroads. Panama has leveraged its superb stewardship of the Canal and central location to create an economic and logistical architecture that is now yielding comparatively stellar economic growth and a substantial reduction in poverty. However, opportunities created by the growth remain elusive to many Panamanians due to continued income inequality fostered by lack of access to quality education and inadequate public infrastructure (especially transportation and health).

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May 3 Elections  
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¶2. (SBU) Panama held general elections on May 3, to elect the President of the Republic and every elected position in the country. Businessman Ricardo Martinelli won a landslide victory, gaining 60% of the vote, and his "Alliance for Change" coalition won a comfortable majority in the National Assembly. The alliance features Martinelli's own Democratic Change (CD) party, the Panamenista Party, led by his Vice President-elect and Foreign Minister-designate Juan Carlos Varela, the Patriotic Union (UP) party, and the MOLIRENA party. Martinelli's government and the new National Assembly will be sworn in on July 1. The governing Revolutionary Democratic Party (PRD) was badly defeated, and is mired in mutual recrimination among several leaders trying to establish their leadership as the party prepares to rebuild. The outgoing government has maintained excellent ties with the USG, and there is every reason to believe relations will continue to be close under the new government.

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Booming Economy  
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¶3. (SBU) Panama's economic foundation is the Canal through which passes roughly 5% of world commerce. The Panama Canal Authority (ACP) has embarked on a \$5.25 billion dollar expansion, the centerpiece of which is a third set of locks capable of handling the largest class of container vessels. A growing network of ports, including Manzanillo International Terminal in Colon (partially owned by U.S. firm Carrix), facilitates trans-isthmian logistics along with revitalized Kansas City Southern Railway between Panama City and Colon. Panama Ports (Hutchison Port Holdings, Inc. of Hong Kong) launched a \$240 million expansion of its Pacific and Caribbean terminals, augmenting the GOP's construction of the \$215 million Panama-Colon Highway. The Colon Free Zone generated over \$19 billion in trade last year. It serves as a hemispheric "one-stop shop" for sourcing, financing, and delivering products (mostly from Asia) to Latin American markets. Panama's robust financial center, with 90 banks and \$63 billion in assets fuels the purchase and movement of cargo and facilitates the absorption of robust foreign direct investment (FDI) inflows that totaled \$2.4 billion for 2008. Through generally prudent management, it has been able to finance construction projects and consumer spending, key drivers of GDP growth - 11.5% in 2007 and roughly 9% in 2008. Although the global financial crisis will impact Panama, growth is expected to be 1-3% - one of the only countries in the hemisphere expecting positive growth.

¶4. (SBU) In recent years, Panama has reached beyond its traditional maritime and financial networks to build connectivity of data and knowledge, and people. Panama lies at the junction of five high bandwidth submarine fiber optic cables, placing Panama City second only to New York City in bandwidth availability. This feature was key in the decisions of Dell and Hewlett-Packard to locate regional headquarters at the former Howard Air Base, which is undergoing a \$705 million transformation as a regional manufacturing and distribution hub. Panama's tourism industry has similarly mushroomed in the past five years, with tourist arrivals increasing from 600,000 to 1.6 million between 2000 and 2008. Arrivals at Tocumen International Airport reflect a similar trend, climbing from over 2.1 million in 2000 to an estimated 4.5 million in 2008. Tocumen recently completed an \$85 million expansion of its international terminal, complimented by the concurrent growth in its flag carrier, Copa (which codeshares with Continental Airlines).

¶5. (SBU) A recent United Nations report highlighted true progress in poverty reduction from 2001 to 2007 - overall poverty fell from 37% to 29% and extreme poverty fell from 19% to 12%. Yet, the distribution of Panama's wealth and income remains highly skewed, and Panama has one of the highest degrees of inequality in the Americas. This situation creates palpable resentment as BMWs and Land Rovers zip past hot, crowded, buses that subject riders to unreliable multi-hour commutes. Most inhabitants of Panama City have never visited an indigenous area or the Darien where poverty predominates, and government services are minimal.

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MERIDA and PANAMA  
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¶6. (SBU) Though it is in the transit zone for narcotic smuggling and has large amounts of drugs flowing through its territorial waters, Panama has taken decisive action against drug traffickers, and is one of the top countries in Latin America in terms of drug seizures, with 60 tons seized in 2007, 51 seized last year, and 23 tons seized so far this year. This is due primarily to its excellent collaborative counter-narcotics relationship with the U.S., and the work of a small group of elite police officers. Major international drug trafficking organizations from Colombia and Mexico are present in Panama, as is the FARC's 57th Front, which traffics drugs and weapons through Panama.

¶7. (SBU) While Panama's security apparatus racks up

impressive drug seizures, the Panamanian public is alarmed by a perceived wave of crime and insecurity. Constant killings among drug traffickers and a growing indigenous youth gang problem have left the public feeling uneasy in this traditionally low-crime country. Taking advantage of Merida Initiative funds, Embassy Panama is implementing an integrated inter-agency approach to the problem. The foundation for our strategy is community policing. Post is working with the Panamanian National Police (PNP) to implement a Community Policing strategy, in conjunction with the Miami Dade Police Department, to train the highest level of the police leadership in the concept of community policing. Community organizations are also being established to interact with the police, not just to identify criminal activities, but to report on police corruption and malfeasance. Post will use additional funds allotted through Merida to strengthen the PNP's ability to investigate and discipline internal corruption as a prerequisite for effective community policing. In addition, USAID Panama will use Merida funds to develop youth centers in high risk areas, in conjunction with Panamanian NGOs and faith-based organizations, which will provide vocational training, extra-curricular activities, safe-haven recreational activities.

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Security/Counter-Terrorism  
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18. (SBU) Panama's main terrorism concern is an attack against the Canal. The Panama Canal Authority and the Government of Panama work closely together to protect the Canal, and the Embassy's Office of Defense Cooperation (ODC) has trained several elite squads of security forces to support protection of the Canal in the event of an attack. Panama co-hosts the annual PANAMAX exercise, a multinational security training exercise tailored to the defense of the Panama Canal. The exercise replicates real world threats to the Canal in order to develop appropriate responses and guarantee safe passage to the approaches to the canal and through the waterway. Twenty nations, including the United States, participate. On the margins of PANAMAX, Panama hosts a tabletop exercise specifically designed to enhance its ability to address asymmetric threats.

19. (SBU) Panama's other main terrorism concern is the presence of drug trafficking organizations (DTOs) and elements of the FARC in the Darien. With a population of no more than 50,000 and only one main road, the Darien is a very underdeveloped region on the border with Colombia, which is physically and psychologically remote for most Panamanians. Elements of the FARC have long used the parts of this region closest to the border as a rest and relaxation zone, in addition to organizing drug trafficking and logistical operations in support of other FARC units inside of Colombia. In trying to confront this threat, Panama is limited by the fact that it has no military forces, following their dissolution after Operation Just Cause in 1989. Panama's security is the responsibility of the Panamanian National Police (PNP), the National Aero-Naval Service (SENAN), the National Frontier Service (SENAFRONT), and the Institutional Protection Service (SPI, a Secret Service equivalent). The Torrijos government spun SENAFRONT off from the PNP late last year in an attempt to stand up a more capable force on the border that could keep the DTOs and the FARC under control. While this was a good first step, SENAFRONT is still far away in terms of size, training and equipment from being able to take on the FARC. Post, through our Narcotics Affairs Section (NAS) and ODC, has been working with limited funds to assist the development of SENAFRONT with training and equipment.

110. (SBU) Post is developing a proposal for DOD counter-insurgency funds that would stress a "whole of government" strategy, based on the idea that the real danger of the FARC and DTOs in the Darien is that they may be able to usurp the legitimacy of the state in an area where the state had little effective presence beyond the main road and a few SENAFRONT bases, and the FARC and DTOs are able to buy

consciences by paying premium prices for goods and assistance with the drug trade. The funds would be used to leverage GOP funds and spearhead an effort to develop effective techniques for improving government services in remote areas. This program would go hand in hand with other DOD funded programs to improve SENAFRONT's logistical capabilities so it could cut the drug, weapons and supply trafficking routes in the Darien.

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Homeland Security Cooperation  
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¶11. (SBU) Post's Country Team features representatives of ICE, CBP, and CIS. ICE has recently developed a vetted unit within the PNP, funded by State Department Narcotics Affairs Section (NAS) funds. This unit has already had several successes and is expanding the Embassy's ability to investigate and combat the organizations trafficking in weapons, money and people. ICE is also working to develop a Trade Transparency Unit (TTU) together with the Panamanian Customs Authority. This program would allow the GOP and ICE/CBP to get a much better understanding of the trade patterns in Panama, and especially into and out of the Colon Free Zone (the second largest in the world). At the same time, CBP has been working with SENAFRONT and other Panamanian security services to man a checkpoint on the Pan-American Highway to try to stop the flow of drugs and other illegal contraband along this critical roadway. They have also brought teams down from the Border Patrol, funded by NAS, to work with SENAFRONT and develop its professional skills.

¶12. (SBU) One of the most important Homeland Security programs in Panama is the Container Security Initiative (CSI), a joint CBP and ICE program, which currently features three scanners at Panama's three busiest ports scanning containers heading to the U.S. and CBP officers in-country assisting in the ports. The GOP was so impressed with this program that it bought nine additional scanners to scan additional containers at additional ports.

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Torrijos wants the FTA  
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¶13. (SBU) President Torrijos, who leaves office July 1, asserts he fulfilled all major campaign promises, but one - the FTA. The FTA is a legacy issue; President Torrijos desires a 'book-end' to his father's Canal treaties. Thus President Torrijos and his administration are willing to spend political capital to legislatively address labor and bearer share issues brought up by the U.S. legislative and executive branches. However, this late in his administration, that capital is rapidly diminishing. The choreography of the potential movement of the FTA through Congress and synchronization with potential Panamanian reforms is difficult. The U.S. legislative and executive branches must signal to the Panamanians that the U.S. Congress will vote on the FTA in order to rally the PRD majority in the National Assembly to pass legislation on labor issues and bearer shares during the Panamanian lame duck session, before the July 1 transfer of power. Torrijos has already issued three executive decrees instituting labor reforms. But the rest of the issues require National Assembly action, and the legislation is politically difficult. On labor, President Torrijos' center-left majority can muster the votes, but cannot appear to be kowtowing to the United States. On bearer shares, the Torrijos Administration faces powerful and persistent opposition by lawyers who issue those shares, two of whom are former Panamanian ambassadors to the United States, and many of whom are stalwart contributors to the PRD.

¶14. (SBU) After July 1, a new Administration assumes power. The incoming Martinelli administration, thanks to lobbying from Obama administration officials and G-20/OECD pressure, has already agreed to start TIEA negotiations in 2009.

However, that agreement is fragile, especially in light of recent statements by Obama administration officials that seem to indicate a reconsideration of U.S. trade policy as a whole, including forward movement on the Panama FTA. It would also be very difficult for Martinelli's administration to take on the labor reforms. Martinelli's administration, based on a small and weak party (Democratic Change), will spend considerable effort merely maintaining an unwieldy four party coalition to govern. His coalition might very well splinter if forced to vote on labor reforms, and complex issues will be difficult to deal with as the government assembles its team and learns to work together. A failed FTA will be a blow to reformers and will strengthen both traditional and nationalist voices in Panama and those in a new generation who simply call for fewer American-centric policies. Failure could also increase uncertainty about the \$6.2 billion stock of U.S. investment in Panama.

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Panamanian Reforms - Tax Haven  
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¶15. (SBU) Many sources have labeled Panama as a tax haven. However, Panama is not the stereotypical post office box destination for corporations seeking to avoid U.S. taxation. Rather, the vast majority of U.S. companies that locate subsidiaries in Panama do so to expand market share in Latin America. U.S. businesses are attracted to Panama due to the use of the U.S. dollar, modern banking system, the Colon Free Zone, and transportation/logistical architecture that includes the Panama Canal, Panama Canal railroad, major ports, and a regional air hub. Companies use Panama as a marketing and distribution platform to expand brand awareness and sales in the region, often leading to increased employment in the United States.

¶16. (SBU) The reason Panama does not fit into this stereotype is that Panama has effective anti-money laundering/anti-terrorist finance banking regulation. However, transparency issues remain, concentrated in the corporate practices of Panama's loosely regulated legal profession. Under Panamanian law, lawyers are the only group empowered to establish corporations, including shell corporations that issue bearer shares. Bearer shares serve as an extremely powerful 'cloaking device' for financial crimes. Held anonymously by "the bearer," these instruments allow the persons possessing them to store and transfer funds with little risk of detection. Often wealthy individuals or companies will open an "anonymous society" corporation in Panama. The President and Directors of the company are random people paid a nominal sum to sign a legal document that allows them to be the "leadership" of the anonymous society corporation. However, true ownership lies in the person who physically controls the bearer shares. The person who physically controls bearer shares likely will not be able to deposit them in a Panamanian bank without strict disclosure requirements, as the banks are tightly bound by know-your-customer rules. However, nothing stops bearer shares holders from traveling to a country with lax banking regulations and opening bank accounts through an attorney or other proxy (who can hide the identity of the holder of the bearer shares).

¶17. (SBU) After substantial engagement from the U.S. Government, the Government of Panama announced on April 7 that it intends to regulate bearer shares. This breakthrough, when fully executed, will fulfill the USG's most prominent financial crimes regulatory recommendation, and remedy Panama's sole grave remaining anti-money laundering/counter-terrorism finance (AML/CFT) deficiency.

¶18. (U) End Scenesetter.  
STEPHENSON